REVISED INVESTMENT POLICY FOR THE HOUSING AUTHORITY OF THE CITY OF ARLINGTON, TEXAS NOVEMBER 7, 2007

Section I. Policy Statement

It is the policy of the Housing Authority of the City of Arlington, also known as the Arlington Housing Authority (AHA), that after allowing for the anticipated cash flow requirements of the AHA and giving due consideration to the safety and risk of investment, all available funds shall be invested in accordance with the investment guidelines issued by the U.S. Department of Housing and Urban Development (HUD) [Attachment: PIH Notice 96-33 and 2001-7] and within the parameters of Chapter 2256 of the Government Code (Texas Public Funds Investment Act).

Effective cash management is recognized as essential to good fiscal management. Interest from investments is a source of revenue to the AHA. The AHA's investment portfolio shall be managed in a manner designed to maximize this revenue source, to be responsive to public trust, and to be in compliance with legal requirements and limitations.

Section II. General

A. Investment Purpose

The purpose of this investment policy is to comply with both HUD requirements and the Texas Public Funds Investment Act. The AHA is required to adopt a written investment policy regarding the investment of its funds and funds under its control. This investment policy addresses the methods, procedures, and practices that must be exercised to ensure effective and judicious fiscal management of the AHA's funds. This investment policy shall be implemented by the AHA's Board of Commissioners acting through the Executive Director of the AHA. The Executive Director, or his or her designee, shall, in all instances, act in accordance with this investment policy and the directives of the Board of Commissioners of the AHA.

B. Investment Objectives

The AHA shall manage and invest its cash with consideration of six objectives including: safety, yield, liquidity, maturity, amount, and administrative cost. The determination of the best or appropriate types and mixtures of investments is dependent on these objectives. The investment portfolio should be consistent with the goals of the AHA's cash management program and directive of the Board of Commissioners. The objectives are discussed in further detail as follows:

1. Safety. Safety of principal is the foremost objective of the investments. Safety is achieved through adherence to the permitted investments which are backed by the full faith and credit of, or a guarantee of principal and interest by the U.S. Government, a government agency or issued by a government-sponsored agency, coupled with an appropriate maturity date.
   a. Credit risk can be minimized by:

- Limiting investments to the safest type of investments;
- Pre-qualifying the financial institutions and broker/dealers with which the AHA will do business; and
- Diversifying the investment portfolio so that potential losses on individual issuers will be minimized.

b. Interest rate risk can be managed by limiting the maximum weighted average maturity of the investment portfolio to 365 days. In addition, the AHA will:
   - Structure the investment portfolio so that investments meet cash requirements for ongoing operations;
   - Invest operating funds primarily in certificates of deposit, shorter-term securities, money market funds, or local government investment pools; and
   - Diversify maturities and staggering purchase dates to minimize the impact of market movements over time.

2. Yield. The AHA will strive to achieve the highest yield consistent with the other objectives of this investment policy. The investment portfolio shall be designed with the objective of attaining a market rate of return through budgetary and economic cycles, taking into account the investment risk constraints and liquidity needs. Tax-exempt securities are not appropriate for investment by the AHA because it would not benefit from the tax advantage.

3. Liquidity. All investments must be capable of being liquidated on one day's notice. Therefore, no investments may be made which impose a longer notice period for redemption or which are not readily marketable. Because all possible cash demands cannot be anticipated, a portion of the portfolio should be invested in shares of money market funds or local government investment pools that offer same day liquidity.

4. Maturity. Investments should be scheduled to mature when funds are needed. Sales of securities prior to maturity should be avoided due to the inherent risk. (If the market interest rate increases above the yield on the investment, the market value of the securities will decline.) Investments of general funds shall be limited to securities with maturity in periods of up to one year, or such lesser period that coincides with expected disbursements by the AHA, but not beyond the current financing cycle. AHA may invest administrative fee reserves in securities having maturities up to three years.

5. Amount. The best or most appropriate type of investment depends, to some degree, on the amount available for investment because certain investments require a large initial amount.

6. Administrative Cost. In choosing an investment, the AHA will consider the administrative work involved, particularly with regard to investments of short duration. Substantial amounts can be invested for periods as short as one or two days. However, the administrative costs with small amounts may be greater than the return on the investment, thus would not be justified or cost effective. Administrative costs will be higher with a more frequent

turnover of investments and must be taken into account together with the yield and term in determining the optimum investment strategy.

C. Review of Policy

The AHA Board of Commissioners shall review this investment policy and provide direction in regards to investment strategies at least annually. The board shall adopt a resolution stating that it has reviewed the policy and investment strategies annually, approving any changes or modifications.

D. Reporting

1. The Executive Director or designee shall prepare an investment report on a quarterly basis that summarizes investment strategies employed in the most recent quarter and describes the portfolio in terms of investment securities, maturities, and shall explain the total investment return for the quarter. Not less than quarterly, the Executive Director or designee shall prepare and submit to the AHA's Board of Commissioners a written report of investment transactions for all funds covered by this investment policy for the preceding reporting period.

2. The investment report must:

    a. Include a statement of compliance of the AHA's investment portfolio with state law and the investment strategy and policy approved by the Board;

    b. be prepared by the Executive Director of the AHA or his/her designee;

    c. be signed by the Executive Director of the AHA; and

    d. contain a summary report of each fund group that reflects the:

        (1) a listing of individual securities held at the end of the reporting period;

        (2) beginning and ending book and market value of securities for the period;

        (3) additions and changes to the market value during the period;

        (4) average weighted yield to maturity of portfolio as compared to applicable benchmark;

        (5) listing of investment by maturity date;

        (6) fully accrued interest for the reporting period; and

        (7) percentage of the portfolio that each type of investment represents;

3. The report shall be presented not less than quarterly to the AHA's Board of Commissioners within a reasonable time after the end of the period.

E. Audit

The AHA, in conjunction with its annual financial audit, shall perform a compliance audit of management controls on investments and adherence to this investment policy.

F. Responsibility and Control

1. Investments shall be made with judgment and care, under prevailing circumstances, that a person of prudence, discretion and intelligence would exercise in the management of the person's own affairs, not for speculation, but for investment, considering the probable safety of capital and the probable income to be derived. Investment of funds shall be governed by the investment objectives listed in Section II. B. of this policy.

2. In accordance with HUD regulations and the Public Funds Investment Act, the Board designates the Executive Director as the AHA's Investment Officer. The Executive Director may, at his or her discretion, assign investment responsibilities to AHA management staff, to act as the Investment Officer on behalf of the Executive Director. An Investment Officer is authorized to execute investment transactions on behalf of the AHA. No person may engage in an investment transaction or the management of AHA funds except as provided under the terms of this policy as approved by the Board. The investment authority granted to the investing officers is effective until rescinded by the Board.

3. The Investment Officer, acting in accordance with written procedures and exercising due diligence, shall not be held personally responsible for a specific investment's credit risk or market price changes, provided that these deviations are reported immediately and the appropriate action is taken to control adverse developments.

4. The AHA will implement the following internal controls to assist in controlling investments and preventing loss or misuse:

   a. Investment transactions shall be authorized by the AHA Board of Commissioners and documented in the board minutes.
   b. Investment documents shall be kept in a safe fire-resistant locked file cabinet, safe deposit box, or other similarly secured location.
   c. Individuals responsible for custody of securities shall be someone other than an individual maintaining the accounting records.
   d. Investments shall be maintained in a custodian or trust account.
   e. Investments shall be in the name of the AHA
   f. Investments shall be recorded in detail in an investment ledger.
   g. A system shall be in place to insure that all interest earned is collected and credited to the appropriate AHA records.
   h. Investments shall be reconciled at least quarterly to the detailed record (investment ledger).
   i. Written confirmation for telephone (voice) transactions for investments and wire transfers.

G. Ethics and Conflicts of Interest

1. Officers and employees involved in the investment process shall refrain from personal business activity that could conflict with the proper execution of the investment program, or which could impair the ability to make impartial investment decisions. The Investment Officer shall disclose to the Board of Commissioners of the AHA any material financial interest in financial institutions that conduct business with the AHA. The Investment Officer shall further disclose any personal financial investment positions that could be related to the investments of the AHA, particularly with regard to the timing of purchases and sales of investments. Ethics policies promulgated by the federal government, the State of Texas and/or the AHA shall be strictly followed.

2. An Investment Officer of the AHA who has a personal business relationship with an entity seeking to sell an investment to the AHA shall file a statement disclosing that personal business interest. The Investment Officer who is related within the second degree by affinity or consanguinity to an individual seeking to sell an investment to the AHA shall file a statement disclosing that relationship. A statement required under this subsection must be filed with the Texas Ethics Commission and the AHA's Board of Commissioners.

H. Investment Training

1. The Investment Officer shall attend at least one training session relating to the officer's responsibilities under this investment policy within 6 months after taking office or assuming duties and thereafter no less often than once every two years, as required by Chapter 2256 of the Texas Government Code.

2. Training under this section must include at least 10 hours of instruction relating to investment responsibilities. The investment training session shall be provided by an independent source. Investment education topics include investment controls, security risks, strategy risks, market risks, and compliance with this investment policy.

I. Authorized Financial Institutions

1. The Investment Officer shall, at least annually, maintain, review, revise, and adopt a list of financial broker/dealers and financial institutions (collectively "Institutions") authorized to engage in investment transactions with the AHA.

2. All institutions who desire to become qualified bidders for investment transactions must supply the Investment Officer with a completed broker/dealer questionnaire that provides information regarding creditworthiness, experience and reputation and a certification stating the firm has received, read, and understood the AHA's investment policy and agree to comply with the policy. All investment providers, including financial institutions, banks, money market funds, and local government investment pools, must sign a certification acknowledging that the

organization has received and reviewed the AHA's investment policy and that reasonable procedures and controls have been implemented to preclude investment transactions that are not authorized by the AHA's policy.

3. The Investment Officer will make investment selections based on the six objectives outlined in Section II. Part B from the qualified bidders list.

Section III. Investment of Funds

A. Funds Available for Investment

As a general rule, the average amount on deposit in the general fund cash accounts (the targeted maximum cash balance) should be the amount needed on hand for transaction purposes or as a safeguard against cash shortages.

B. Approved Investment Securities

The AHA may only invest in the following investments that are approved by HUD:

1. Direct Obligations of the Federal Government Backed by the Full Faith and Credit of the United States:
   a. U.S. Treasury Bills
   b. U.S. Treasury Notes and Bonds

2. Obligations of Federal Government Agencies
   a. Federal Financing Bank (FFB)
   b. Government National Mortgage Association (GNMA) Mortgage-Backed Securities (GNMA I and GNMA II)
   c. GNMA Mortgage-Backed Securities Program Mortgage-Backed Bonds (MBS)
   d. GNMA Participation Certificates
   e. Maritime Administration Merchant Marine Bonds, Notes and Obligations
   f. Small Business Administration (SBA) Small Business Investment Corporation (SBIC) Debentures
   g. Tennessee Valley Authority (TVA) Power Bonds and Notes

3. Securities of Government-Sponsored Agencies
   a. Farm Credit Consolidated System-Wide Discount Notes
   b. Federal Farm Credit Banks Consolidated System-Wide Bonds
   c. Federal Land Banks Consolidated Bonds
   d. Federal Home Loan Banks Consolidated Obligations
   e. FHLMC Mortgage Participation Certificates (PC) (Guaranteed)
   f. FHLMC Collateralized Mortgage Obligations (CMOs)
   g. Federal National Mortgage Association (FNMA) Debentures
   h. FNMA Notes
   i. FNMA Short-term Discount Notes
   j. FNMA Capital Debentures
   k. Student Loan Marketing Association (SLMA) Obligations

4. Others
    a. Demand and Savings Deposits
    b. Money-Market Deposit Accounts
    c. Municipal Depository Fund
    d. Super NOW Accounts
    e. Certificates of Deposit
    f. Repurchase Agreements
    g. Sweep Accounts
    h. Separate Trading of Registered Interest and Principal of Securities
    i. Mutual Funds
    j. Eurodollar denominated deposits are not acceptable as investment instruments.

C. Investment Register

The AHA or its agent shall maintain an investment register or other record. The register/record shall be maintained in such a manner that a determination can be made as to the amount of investments purchased from each fund and at a minimum provide for recording a complete description of the investment instrument, the date of purchase, its purchase price, its interest rate, and the applicable date of sale or maturity.

D. Bids for Certificates of Deposit

Bids for certificates of deposit may be solicited:
1. orally
2. in writing
3. electronically, or
4. in any combination of the foregoing methods

Section IV. Cash Management

A. Cash Management by the AHA

1. Good cash management, which is an objective of the AHA's management, creates responsibilities for the use of funds. The primary goals of cash management are to assure the availability of cash for transaction needs, preserve the value of cash resources and earn the maximum return on funds until disbursed.

2. The AHA will monitor returns of the cash managed by agents. If the AHA finds that administrative costs of an in-house program are such that the net yield on investments is less than that obtainable through an alternative, the AHA will consider that alternative.

B. Cash Management by an Agent

1. As an alternative to an in-house cash management program the AHA may enter into a contract with an approved governmental unit such as a state agency established for this purpose or another public housing authority, or a financial institution (excluding investment bankers and brokerage houses) to administer its cash management program.

2. Such programs may include any of the functions of cash management, i.e. receipts, disbursements and investments. Such a contractual arrangement will give the AHA the expertise and administrative skills which it would not otherwise be expected to have and often can make a cash management program cost-effective.

Section V. Banking Services

Banking services shall be arranged by selecting a bank through competitive solicitation to assure the AHA that it receives the banking services provided at the lowest costs. The AHA will designate a single bank account for the deposit of all payments that are received from HUD through direct deposit-electronic funds transfer. Banking services shall be periodically solicited through competitive negotiation.

Section VI. Collateralization

The AHA shall require its depositories to continuously and fully (100%) secure all deposits regardless of type (i.e. regular savings, etc.) that are in excess of the $100,000.00 insured amount. This may be accomplished by the pledging or setting aside collateral of identifiable U.S. Government securities as prescribed by HUD. The AHA must have possession of the securities or an independent custodian must hold the securities on behalf of the AHA as a bailee, as evidenced by safekeeping receipt and a written bailment for wire contract and will be maintained for the full term of the deposit. Such securities shall be owned by the depository and the manner of collateralization shall provide the AHA with a continuing perfected security interest for the full term of the deposit in the collateral in accordance with applicable federal and state laws and regulations. Such collateral shall, at all times, have a market value at least equal to the amount of the deposits so secured.

Section VII. Exemption

Any investment currently held that does not meet the guidelines of this policy shall be exempted from the requirements contained herein. At maturity or liquidation, such funds shall be reinvested only as provided by this policy.

Section VIII. Legal Guidelines and Parameters

The guidelines of HUD Notice 95-27, issued May 11, 1995, and the parameters found in the Public Funds Investment Act, Chapter 2256, Texas Government Code, including any amendments or successor provisions thereto, are incorporated herein by the reference and shall control to the extent there exists any inconsistency between this investment policy and such guidelines or parameters.

Section IX. Notification

The investment policy will be forwarded annually to the investment agents acting on behalf of the AHA. This is intended to inform them of the investment policies and guidelines of the AHA to ensure that they have implemented reasonable procedures and controls designed to fulfill those objections and conditions. This will include informing the investment agents of the Authority's investment horizons, limitations, and strategy and risk constraints.

ATTACHMENTS

1. PIH Notice 96-33
2. PIH Notice 2001-7

PUBLIC HOUSING AGENCIES; INDIAN NOTICE PIH 96-33(HA)

Housing Authorities; Secretary's Issued: June 4, 1996 Representatives; State/Area Expires: June 30, 1997. Coordinators; Directors, Public Housing Divisions; Administrators, Offices of Native American Programs; Resident Management Corporations (RMCs)

Required HA Cash Management and Investment Policies and Procedures

1. PURPOSE

The purpose of this Notice is to advise public housing agencies and Indian housing authorities (herein referred to as HAs) and Area Offices of the Department's HA requirements governing cash management and approved investment instruments. The Notice extends and reissues, with minor editorial changes, the policies and procedures, including the list of HUD approved investment instruments, previously set forth in Notice PIH 95-27.

2. BACKGROUND

The Annual Contributions Contract (ACC) requires the HA to deposit and invest all program funds for projects under an ACC in accordance with the terms of a General Depository Agreement. The General Depository Agreement must be in a form approved by HUD and is executed between the HA and the depository. In addition, the ACC requires the HA to invest General Fund (program) monies only in HUD approved investments.

The Federal Code of Regulations, Part 85, Subpart C, (24 CFR § 85.20) requires HAs to establish cash management procedures. Cash management is the process of managing the cash flow of a HA to optimize its use of funds. This process involves the timing of receipts and disbursements to assure the availability of funds to meet expenditures and to maximize the yield from the investment of temporarily surplus funds. Effective cash management calls for organized planning. Good relations between the HA and the financial institution can improve the effectiveness of a cash management program.

3. APPLICABILITY

This Notice applies to the Low Rent Public Housing Program, the HA Owned/Leased Housing Homeownership Program (Turnkey III Program), the Section 23 Leased Housing Program, and the Mutual Help Homeownership Program.

4. BANKING SERVICES

Banking services shall be arranged by selecting a bank through competitive solicitation to assure the HA that it receives the banking services provided at the lowest cost. It should be noted, however, that HAs must designate a single bank account for the deposit of all payments that are received from HUD through Direct Deposit-Electronic Funds Transfer (DD-EFT). (A Standard Form 1199A, Direct Deposit Sign-Up Form, must be submitted to designate this account.) A copy of the General Depository Agreement (see below) with the financial institution shall be attached with the SF-1199A. Once the funds are received, they may be transferred to separate accounts according to the applicable program.

a. General Depository Agreement

The General Depository Agreement (Form HUD-51999) shall be executed by the HA and the depository. The depository must be a financial institution whose deposits are insured by the Federal Deposit Insurance Corporation (FDIC) or National Credit Union Share Insurance Fund (NCUSIF). An original HUD-51999 should be maintained by the HA and the financial institution. A copy of the HUD-51999 should be sent to the HUD Area Office and the Field Accounting Office (along with the SF-1199A).

b. Procurement Procedure and Period of Service

Banking services should be periodically solicited through competitive negotiation. The solicitation in the form of a Request for Proposal (RFP) would permit the HA to evaluate the quality of the services received as well as the price. This periodic process should prevent the bank supplying the services from becoming complacent in its dealings with the HA.

5. COLLATERALIZATION OF DEPOSITS

HAs shall require their depositories to continuously and fully (100%) secure all deposits regardless of type (i.e. regular, savings, etc.) that are in excess of the 3 $100,000 insured amount. This may be accomplished by the pledging or setting aside collateral of identifiable U.S. Government securities as prescribed by HUD. The HA has possession of the securities (or the HA will take possession of the securities) or an independent custodian (or an independent third party) holds the securities on behalf of the HA as a bailee (evidenced by safe keeping receipt and a written bailment for wire contract) and will be maintained for the full term of the deposit. Such securities shall be owned by the depository and the manner of collateralization shall provide the HA with a continuing perfected security interest for the full term of the deposit in the collateral in accordance with applicable laws and Federal regulations. Such collateral shall, at all times, have a market value at least equal to the amount of the deposits so secured.

6. INVESTMENT OF FUNDS

a. Funds Available for Investment

1) Funds on deposit in the General Fund are comprised of four components: (1) funds for current transaction purposes, (2) development and/or modernization funds (see #2 below), (3) funds exceeding those necessary for the daily operation of the HA which are considered available for investment and (4) any operating reserve funds. As a general rule, the average amount on deposit in the General Fund cash accounts (the targeted maximum cash balance) should be the amount needed on hand for transaction purposes or as a safeguard against cash shortages. In the interest of good cash management, non-interest bearing deposits should be reduced to the amount necessary to maintain a good banking relationship.

2) Under the Modernization and Development Programs, the term "cash management" also means minimizing the time elapsing between the drawdown and disbursement of funds by the HA. HUD has established the maximum time to be generally three working days. Therefore, reference to "excess funds" also means the amount of modernization or development funds drawn down, but not needed for immediate disbursement (see 24 CFR § 85.21 (b)). Interest income earned on modernization funds is included as operating income in the calculation of operating subsidy eligibility under the Performance Funding System (PFS). Interest income earned on development funds is credited to the development program and reduces the development cost of the project.

b. Approved Investment Securities

In most cases, purchases of securities shall have maturities which coincide with expected disbursements by the HA. For the purpose of investing operating reserves, issues shall be limited to maturities three years or less. Although some of the following securities have maturities longer than three years, they can be traded in the secondary market. A list of investments approved by HUD for the investment of HA funds is attached. HAs are required to choose from these financial instruments. Within the HUD approved instruments, HAs are permitted to modify their investment policy without prior HUD approvals. The choice of investments from the approved list should be made using the criteria developed in the remainder of this paragraph.

c. Determination of Investment Type

The determination of the best or appropriate types and mixtures of investments is dependent on several factors. The primary objective is safety. Once that objective is attained, the optimum return on the investment should be consistent with the goals of the cash management program of the HA. The factors that should be taken into account include the following:

(1) Safety - Safety is achieved through adherence to the list of permitted investments which are backed by the full faith and credit of, or a guarantee of principal and interest by, the U.S. Government, a Government agency or issued by a Government-sponsored agency, coupled with an appropriate maturity date.

(2) Yield - The HA should strive to achieve the highest yield consistent with the other factors of the investment policy. Tax-exempt securities are not appropriate for investment by a HA because it would not benefit from the tax advantage.

(3) Liquidity - All investments must be capable of being liquidated on one day's notice. Therefore, no investments may be made which impose a longer notice period for redemption or which are not readily marketable.

(4) Maturity - Investments should be scheduled to mature when the funds are needed. Sale of securities prior to maturity should be avoided due to the inherent risk. (If the market interest rate increases above the yield on the investment, the market value of the securities will decline.) Investments shall be limited to securities maturing in periods of up to one year, or such lesser period that coincides with expected disbursements by the HA, but not beyond the current financing cycle. HAs may invest in securities up to three years for the investment of operating reserves.

(5) Amount - The best or most appropriate type of investment depends, to some degree, on the amount available for investment because certain investments require a large initial amount.

(6) Administrative Cost - In choosing an investment, a HA must consider the administrative work involved, particularly with regard to investments of short duration. Substantial amounts can be invested for periods as short as one or two days. However, the administrative costs with small amounts may be greater than the return on the investment, thus would not be justified or cost effective. Administrative costs will be higher with a more frequent turnover of investments and must be taken into account together with the yield and term in determining the optimum investment strategy.

d. INVESTMENT OF FUNDS HELD BY HA FISCAL AGENTS

Funds held by the Fiscal Agent in any trust funds shall be invested in strict accordance with the Resolution establishing such funds. Where the Resolution contains no provision concerning the investment of funds, the funds shall be invested in securities approved for General Fund Investment provided such investment will mature or may be redeemed at the option of the purchaser at not less than the purchase price on or prior to the date such funds are required to be disbursed by the Fiscal Agent. A description of funds established by HA resolutions authorizing the issues of bonds is attached.

e. Investment Register

An investment register or other record shall be maintained by the HA or its agent. The register/record shall be maintained in such a manner that a determination can be made as to the amount of investment securities purchased from each fund and at a minimum provide for recording a complete description of investment instrument, date of purchase, purchase price, interest rate, and applicable date of sale or maturity. The investment register/record may also be used to identify the source of funds invested (i.e., modernization or development funds, tenant security deposit funds, operating funds).

f. Internal Controls
HAs shall implement the following internal controls to assist in controlling investments and preventing loss or misuse.
(1) Investment transactions shall be authorized by the HA governing board and documented in the board minutes.
(2) Investment documents shall be kept in a safe fire-resistant locked file cabinet, safe deposit box, or other similarly secured location.
(3) Individuals responsible for custody of securities shall be someone other than an individual maintaining the accounting records.
(4) Investments shall be maintained in a custodian or trust account.
(5) Investments shall be in the name of the HA.
(6) Investments shall be recorded in detail in an investment ledger.
(7) A system shall be in place to insure that all interest earned is collected and credited to the appropriate HA records.
(8) Investments shall be reconciled periodically to the detailed record (investment ledger).

7. CASH MANAGEMENT
A major factor contributing to the success of an investment program is the delegation of responsibility and authority for developing and executing it. A HA should compare the cost of establishing a cash management program in-house (if qualified professional staff are available) to contracting out. If HAs contract for cash management and investment services, then the organization should have qualified personnel to achieve cost-effectiveness. Commercial banks and savings and loans association offer such services.

Good cash management, which is an objective of management, creates responsibilities for the use of funds. Such responsibilities are placed on both the HA and HUD for a successful program to benefit both. The primary goals of cash management are to assure the availability of cash for transaction needs, preserve the value of cash resources and earn the maximum return on funds until disbursed.
a. Cash Management by the HA
The HA should compare the return from an in-house cash management program with a program managed by an agent. If the HA finds that administrative costs of an in-house program are such that the net yield on investments is less than that obtainable through an alternative, the general rule is that the HA should use that alternative.
b. Cash Management by an Agent
As an alternative to an in-house cash management program, a HA may enter into a contract with an approved governmental unit such as a State agency established for this purpose (see attachment A, #6, Municipal Depository Fund), or a financial institution (excluding investment bankers and brokerage houses) to administer its cash management program. Such a program may include any of the functions of cash management, i.e., receipts, disbursements and investments. Such a contractual arrangement will give a small HA the expertise and administrative skills which it would not otherwise be expected to have and often can make a cash management program cost-effective.
c. Temporary Funds Available for Investment
(1) Each HA with an average cash balance of $20,000 or more shall invest such funds in HUD-Approved Investment Securities in order to meet the PFS Target Investment requirements (24 CFR Section 990.109 (e), 24 CFR §950.725 (e)).

HAs with average cash balances of less than $20,000 shall also invest such funds in HUD-Approved Investment Securities. For the purpose of calculating operating subsidy eligibility under the PFS (24 CFR Section 990.109 (e), 24 CFR §950.725 (e)) these HAs shall make a reasonable estimate of investment income for the requested budget year. Please note that investment income estimates for these HAs are not subject to the mandatory year-end adjustment.

(2) See Handbook 7475.13, Performance Funding System (PFS), regarding reporting requirements for projecting investment income for the purpose of calculating PFS operating subsidy eligibility. These requirements mandate a minimum investment income (Target Investment Income) for calculating operating subsidies and allow HAs to retain investment income in excess of the required amount. HAs should review these requirements carefully in developing their cash management programs.

8. MONITORING

The Office of Finance and Budget, PIH, will continue to oversee the overall cash management policy and programs for HAs. Actual monitoring of each HA's cash management will continue to be the responsibility of the respective Area Office.

Monitoring will be accomplished through review of documentation submitted to support the investment income shown in the calculation of operating subsidy and during on-site monitoring reviews.

If there are questions regarding the contents of this Notice, please contact the Office of Finance and Budget at 202-708-1872.

Casimir Bonkowski for Acting
Assistant Secretary for Public and Indian Housing
Attachments

ATTACHMENT A

HUD APPROVED INVESTMENT INSTRUMENTS

1. Direct Obligations of the Federal Government Backed by the Full Faith and Credit of the United States

a. U.S. Treasury Bills

These securities are short-term obligations which a HA or its agent may purchase directly. Treasury Bills with 3- month and 6-month maturities are issued weekly and those with 9-month and 12-month maturities are issued monthly. The minimum denomination is $10,000. They are issued on a discount basis and are redeemed at par upon maturity. U.S. Treasury Bills are available for purchase at any time after issuance from investment departments of banks and from dealers in investment securities. Purchases may be made conveniently using the HA's depository bank. Treasury Bills may be acquired by subscription on the issue date from a Federal Reserve Bank or branch in amounts not in excess of $200,000. Detailed information is contained in the weekly or monthly announcements which may be received regularly upon application to a Federal Reserve Bank or branch.

b. U.S. Treasury Notes and Bonds

These securities are issued periodically by the Treasury Department through Federal Reserve Banks and branches. They are medium to long-term obligations which a HA or its agent can only purchase in the secondary market to assure that they will mature at a date which coincides with scheduled disbursements by the HA. Outstanding issues may be purchased from banks or dealers in investment securities at the market price which on any given day may be more or less than the face amount.

(1) U.S. Treasury Notes

These notes mature in not less than one and not more than 10 years from the issue date and bear interest at fixed rates payable semi-annually.

(2) U.S. Treasury Bonds

These bonds mature after ten years from the issue date and bear interest at fixed rates payable semi- annually. Many issues of bonds are redeemable on call by the Treasury Department before maturity. The yield of such issues usually is computed to the first call date which may be as much as years prior to maturity.

2. Obligations of Federal Government Agencies

a. Federal Financing Bank (FFB)

The Federal Financing Bank is authorized to purchase obligations held by Federal agencies and to issue obligations to the public.

b. Government National Mortgage Association (GNMA), Mortgage- Backed Securities (GNMA I and GNMA II)

The securities, guaranteed by GNMA are issued by an issuer (a GNMA approved mortgage lender). The securities are backed by a pool of government insured or guaranteed mortgages. The holders of the securities receive monthly payments of principal and interest. The minimum denomination issued is $25,000. The difference in GNMA I and GNMA II is that the GNMA II payment date is on the 20th of the month and the GNMA I payment date is on the 15th; GNMA II uses a central paying agency whereas GNMA I has individual issuers sending checks to investors; and GNMA II has interest rates that vary within a one percent range. The maximum maturity for GNMA I and GNMA II is 30 years, except that GNMA I project loans mature in 40 years.

c. GNMA Participation Certificates

These securities, guaranteed by GNMA, were sold by GNMA as the trustee with various other Federal agencies as trusters. They represent beneficial interest in future payments of principal and interest on mortgage pools. Their maturities range between one and 20 years and the minimum denomination is $5,000.

d. Maritime Administration Merchant Marine Bonds, Notes, and Obligations. These securities are issued by shipping companies and are backed by the full faith and credit of the U.S. Government. Each issue is further secured by a first preferred ship or fleet mortgage. Maturities and denominations vary.

e. Small Business Administration (SBA), Small Business Investment Corporation (SBIC) Debentures. When authorized by appropriation acts, the SBA may guarantee principal and interest payments on debentures of SBIC. The SBA may also pool these debentures and sell SBA- guaranteed debentures. These issues have maturities of 10 years and are issued in $10,000 denominations.

f. Tennessee Valley Authority (TVA) Power Bonds and Notes

These securities are secured by a first charge on net power proceeds. Payment of interest and principal on them is ranked ahead of annual payments to the U.S. Treasury. They have been issued in multiples of $1,000.

3. Securities of Government-Sponsored Agencies

a. Farm Credit Consolidated System-Wide Discount Notes

These notes are the secured joint and several obligations of the Farm Credit System which consists of the Federal Land Banks, the Federal Intermediate Credit Banks, and the Banks for Cooperatives. They are issued in denominations of $5,000 and maturities are authorized from 5 to 365 days.

b. Federal Farm Credit Banks Consolidated System-wide Bonds. These bonds are the secured joint and several obligations of the Farm Credit Banks. Their issuance supersedes individual bond issues by the Federal Land Banks, the Federal Intermediate Credit Banks, and the Banks for Cooperatives. They are issued in multiples of $1,000 for maturities in excess of 13 months and in multiples of $5,000 for shorter maturities.

c. Federal Home Loan Banks Consolidated Obligations

These securities are the secured joint and several obligations of the Federal Home Loan Banks comprised of:

(1) Bonds

Bonds which have maturities of one year or more. They are issued in multiples of $10,000, $25,000, $100,000 and $1,000,000.

(2) Notes

Notes which have maturities of less than one year. They are issued in multiples of $10,000, $25,000, $100,000 and $1,000,000.

(3) Discount Notes

Discount notes which have maturities ranging from 30 to 170 days. They are issued in denominations of $100,000 and $1,000,000.

d. FHLMC Mortgage Participation Certificates (PC) (Guaranteed)

These certificates represent undivided interest in specific fixed rate, first lien conventional and residential mortgages. FHLMC provides monthly interest and principal payments. The final payment is the first of the month and year in which the last monthly payment on the last maturing mortgage is scheduled to be paid.

e. FHLMC Collateralized Mortgage Obligations (CMOs)

CMOs are general obligations of FHLMC that are secured by a single pool of conventional mortgages owned by FHLMC. CMOs are issued in several classes with varying stated maturities. Semiannual principal payments are allocated to each class of the CMOs in the order of the stated maturity of each class so that no principal payments are made to holders of a class until classes with an earlier maturity are retired.

f. Federal National Mortgage Association (FNMA) Debentures. These debentures are issued in denominations ranging from $10,000 and with maturities ranging from 20 to 25 years.

g. FNMA Notes

The minimum investment in these notes is $50,000 with maturities ranging from 1 to 20 years.

h. FNMA Short-Term Discount Notes

These notes are similar to commercial paper and are tailored to the individual needs of investors. They are sold at published rates with maturities of 30 to 270 days and in denominations ranging from $5,000.

i. FNMA Capital Debentures

These debentures are subordinated to the non-capital debentures, notes, and short-term discount notes. They were last issued in 1975 in a $10,000 minimum denomination and with maturities of 5 and 25 years.

j. Student Loan Marketing Associations (SLMA) Obligations SLMA issues obligations comprises of guaranteed student loans as follows:

(1) Floating Rate and Master Notes.

These notes bear interest at rates that vary with the 91-day Treasury Bill rate. Short-term borrowing have an original or remaining term maturity of one year or less.

(2) The Series E and F Floating Rate Notes.

These notes bear interest at rates which vary with the 91-day Treasury Bill, except that each issue has fixed minimum and maximum rates known as interest rate "collars" for any quarterly interest period.

(3) Zero Coupon Notes

These notes are shown at net proceeds adjusted for accretion of discount.

4. Demand and Savings Deposits

Demand and savings deposits at commercial banks, mutual savings banks, savings and loan associations and credit unions are permitted for HA funds provided that the entire deposit is insured by the Federal Deposit Insurance Corporation (FDIC) or the National Credit Union Share Insurance Fund (NCUSIF). A deposit in excess of the insurance coverage may be made at a depository institution provided that it is 100 percent collateralized by any of the securities listed under paragraphs 1, 2, and 3 of this Attachment. Care should be taken that withdrawals may be made on demand without loss of interest and without penalty.

5. Money-Market Deposit Accounts

Money-Market Deposit Accounts at depository institutions that may not be insured fully by the FDIC or NCUSIF are permitted provided that the certificates are fully backed by 100 percent collateral consisting of securities listed under paragraphs 1, 2, or 3 of this Attachment. When accounts exceed the $100,000 insurance limitation, their safety also may depend on the HA's control of the underlying collateral which must consist of clearly identified (not pooled) U.S. Government securities. Possession of the collateral securities and a continuous perfected security interest may be the only sure protection against loss in case of financial institution failure.

6. Municipal Depository Fund

A Municipal Depository Fund (Fund) or Local Government Investment Pool which is established by States, municipalities, units of local government or other political subdivisions to serve as an investment fund for HAs is permitted. The securities purchased by a Fund shall be on the HUD-approved list of investment securities. HA shall have either an undivided or divided interest in securities comprising the Fund. The Fund shall be under the control of the Investment Company Act of 1940, and its objective shall be clearly stated. The investment objective of the Fund shall be to obtain as much income as possible consistent with the preservation and conservation of capital. The Fund shall disclose clearly the basis of earnings and how they are distributed. HA shall obtain a statement of potential default and risk and a clear demonstration that withdrawals from the Funds will not be so restricted as to impair a HA's day-to-day cash management 7 needs. The management fee shall be fixed at a reasonable amount and management shall be passive. HA shall limit the amount of funds invested in the Fund to no more than 30 percent of a HA's available investment funds. The Fund shall disclose the relationships of the investment advisor, manager, trustees, custodian and transfer agent. Each financial advisory relationship shall be evidenced by a written document executed prior to, upon, or promptly after the inception of the financial advisory relationship, or promptly after the creation or selection of the issuer. If the issuer does exist or has not been determined at the time the relationship commences, that written document shall set forth the basis of compensation for the financial advisory services to be rendered.

7. Super NOW Accounts
Super NOW accounts have been available and approved for public funds since January 1983. They offer a relatively high market rate and are fully transactional (have no limitations on the number of checks or transfers). Insurance and collateral requirements are as above for subparagraph e Demand and Savings Deposits.

8. Certificates of Deposit
a. Certificates of Deposit are permitted at depository institutions that are insured by an agency of the Federal Government. Caution must be exercised for certificates exceeding the $100,000 insurance limit or when the term is longer than 30-90days. Although the certificates' rate of return may be attractive for larger amounts and longer terms, U.S. Treasury securities offer superior safety and liquidity for the same amounts and terms. Certificates shall be in the HA's name. In addition a General Depository Agreement must be executed by each financial institution that issues a Certificate of Deposit.
b. Certificate amounts above $100,000 are permitted provided that the excess is 100 percent collateralized by clearly identified (not pooled) U.S. Government securities. Possession of the collateral securities and a continuous perfected security interest may be the only sure protection against loss in case of bank failure.
c. Brokered deposits should be avoided because it is impossible to get $100,000 federal insurance on a number of deposits placed by brokers.

9. Repurchase Agreements
Repurchase (repos) agreements for a term not to exceed 30 days may be entered into with Federally insured depository institutions to purchase and sale of securities identified under paragraphs 1, 2, and 3. A repurchase agreement is an agreement negotiated with a bank usually for a short period (1 to 7 days) wherein securities approved for investment are purchased from that bank at a stated price with the bank agreeing to repurchase them on a specified date for a specified amount. The minimum may vary, although it is usually $100,000. There are three main types: (1) fixed term, where both parties are bound to the negotiated time period, (2) demand, where the agreement stays in effect until terminated by either party, and (3) day-to-day, where daily renewal is by mutual consent and 24- hour notice is required for termination. The HA should review existing and future repos for compliance with the following certifications. Prior approval by HUD is not necessary, however, the repos seller depository or its agency must provide a written certification to HUD, Assistant Secretary for Public and Indian Housing (Office of Finance and Budget), the Area Office, and to the HA.

a. that the depository's repo program complies with applicable Federal and State statutes and regulations and that the program does not involve sales or loans of Federal securities by securities dealers that are not regulated or that report to the Federal Reserve Board;
b. that the depository owns the underlying Federal securities (approved for repurchase under HUD guidelines) when the repo interest is sold and that the value of the securities is equal to or greater than the amount the HA pays for the repo;
c. that the HA has possession of the securities (or the HA will take possession of the securities) or an independent custodian (or an independent third party) holds the securities on behalf of the HA as a bailee (evidenced by a safe keeping receipt and a written bailment for hire contract), from the time the repo interest is sold to the HA and will be (or is expected to be) maintained for the full term of the repo;
d. that the repo agreement and any related documents identify specific Federal securities related to the specific repo purchased by the HA;
e. that the repo interest does not represent any interest in a pool or fund of Federal securities for which registration under the Investment Company Act of 1940 may be required;
f. that the HA will have a continuous perfected security interest in the underlying Federal securities under State or Federal law for the full term of the repo (disclosing the method by which perfection has or will be accomplished, i.e., by possession, filing, registration of book-entry securities and/or Federal preemption of State law by Federal regulation);
g. that the depository or a reporting dealer selling the repo has not received any adverse financial report from a credit reporting agency, State or Federal regulatory agency; and
h. that the depository will not substitute other securities as collateral, except to increase the value of the repo security to match the repos's purchase price.

10. Sweep Accounts
Sweep Accounts is a contractual agreement between a bank and a HA which provides that the bank will regularly "sweep" or transfer any available collected balances from the HA's account into repurchase agreements. The Sweep Accounts agreement shall include all the certification provided in the Repurchase Agreement and adherence to paragraph 4-3, Collateralization of Deposits.

11. Separate Trading of Registered Interest and Principal of Securities Separate Trading of Registered Interest and Principal of Securities (STRIPS) are Treasury-based zero-coupon securities which consist of interest or principal on U. S. Treasury securities. STRIPS were issued in minimum increments of $1,000. STRIPS pay no interest until maturity and the rate of return is "locked in" at the time of purchase. The delivery of STRIPS is accomplished by wire transfer through the Federal Reserve book entry system. STRIPS shall be in the name of the HA.

12. Mutual Funds
A Mutual Fund (Fund) is an investment company that makes investments on behalf of individuals and institutions. The Fund pools the money of the investors and buys various securities that are consistent with the Fund's objective.
a. Mutual Fund Criteria. The Fund shall be organized as a no-load, open-end, diversified management company and its shares shall be registered under the Securities Act of 1933. The Fund shall be under the control of the Securities Exchange Act of 1934, Investment Advisers Act of 1940 and the Investment Company Act of 1940. The investment objective of the Fund shall be to obtain as much income as possible consistent with the preservation, conservation and stability of capital. The mutual fund objective cannot be changed without the prior approval of fund shareholders.

b. The securities purchased by the Fund shall be on the HUD-approved list of investment securities. The Fund will not engage in options or financial futures. The HA shall limit the amount of funds invested in the Fund to no more than 20 percent of the HA's available investment funds. The Fund shall disclose clearly the basis of earnings and how they are distributed. The HA shall obtain a statement of potential default and risk. The HA's invested funds shall be accessible to the HA daily. It shall be demonstrated that any limitations on withdrawals will not impair the HA's day-to-day cash management needs. c. The management fee shall be fixed at a reasonable amount. The Fund shall disclose the relationships of the investment advisor, manager, trustee, custodian and transfer agent. The Fund shall clearly state all services (such as wire transfers and check writing privileges) and charges.

d. Investment in the Fund shall be authorized by a Board Resolution. A certified copy of the resolution shall accompany the initial application for the Fund.

e. The Fund (or custodian) and the HA shall sign the General Depository Agreement, HUD-51999 dated June 1991, modified as follows:

(1) In the title, "(Mutual Fund)" shall be added after General Depository Agreement. Whenever "depository" appears in the text it also refers to "mutual fund."

(2) The HA's name and location (including county or city) will be filled in the first clause of the General Depository Agreement. The name, location and the HA's mutual fund account number also will be filled in the first clause. The second clause remains unchanged.

(3) The third clause is substituted as follows: "Whereas, under the terms of the Contract the HA shall invest in a mutual fund (herein called the depository) only on the terms set forth hereafter. Mutual fund is defined as an investment company that makes investments on behalf of individuals and institutions. The depository shall be organized as a no-load, open-end, diversified management company and its shares shall be registered under the Securities Exchange Act of 1933. The depository shall be under the control of the Securities Exchange Act of 1934, the Investment Advisers Act of 1940 and the Investment Company Act of 1940. HA shall acquire shares in a mutual fund whose portfolio includes only securities on the HUD-approved list of investment securities."

(4) Paragraphs 1, 3, 11 and 12 are deleted.

(5) Paragraphs 4 through 6 are modified to read as follows:

(a) Paragraph 4: Any shares purchased from HA funds shall be held by the depository in safe-keeping for the HA until sold. Dividends and distributions on such shares and the proceeds from the sale thereof shall be used to purchase additional shares or remitted directly to the HA.

(b) Paragraph 5: The language "from said Accounts" is deleted.

(c) Paragraph 6: The language "in respect of the Accounts" is deleted.

(d) Paragraphs 7 through 10 are not changed.

(e) The additional language can be typed on a separate page, attached and duly executed. The following language shall be added to the bottom of the page: Page number incorporated in and made a part of the General Depository Agreement between (HA) and (Depository).

ATTACHMENT B

INVESTMENT OF FUNDS HELD BY HA FISCAL AGENTS

Description of Funds
The funds established by HA resolutions authorizing the issuance of bonds to finance the development cost of projects are as follows:

(1) Debt Service Fund
This Fund is established pursuant to the Annual Contributions Contracts and HA Resolutions providing for the issuance of new HA bonds. The Fiscal Agent is explicitly required under the form of the Fiscal Agency Agreement entered into since 1964 to purchase and sell investment securities as the HA, with the approval of the Federal Government, may direct. Where a Fiscal Agency Agreement does not contain a specific requirement for the investment of Debt Service Funds, such investment must, nevertheless, be made since it is a general power and duty of a trustee, (implied if not expressed) to keep funds properly invested in order to attain safety and produce income for the trust funds.

(2) Advance Amortization Fund
(a) Since 1952, the form of Fiscal Agency Agreement in use requires the Fiscal Agent to invest funds on deposit in the Advance Amortization Fund as the HA, with the approval of the Federal Government, may direct.
(b) With respect to the investment of funds resulting from a consolidated sale of bonds by an Agency Authority, only the Agency Authority of HUD may issue investment instructions to the Fiscal Agent. These instructions shall be consistent with HUD guidelines.

(3) Annual Contributions Reduction Account (sometimes called Supplementary Revenues Account); Bond Service Account; Series A Reserve Fund; General Bond Reserve Fund; Rental Debt Service Fund; and Excess Lands Account. The Resolution authorizing Series A and Series B Bonds issued prior to 1951 established these funds and the Resolution usually contains limitations on the investment of funds on deposit in one or more of such accounts.